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20th

ANNUAL

REPORT

1973

Mercantile Bank of Canada



Mercantile Bank of Canada

FINANCIAL HIGHLIGHTS

	1973	1972
TOTAL ASSETS	\$587,244,104	\$390,004,078
TOTAL LOANS	450,920,000	332,952,363
TOTAL REVENUE	41,859,058	24,840,819
BALANCE OF REVENUE	6,540,483	4,703,393
BALANCE OF PROFITS FOR THE YEAR	3,584,483	2,458,393
BALANCE OF PROFITS PER SHARE, based on average shares outstanding	84.4¢	95.2¢

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DIRECTORS AND OFFICERS

PAUL H. AUSTIN
President
Mercantile Bank of Canada

ANDRÉ BACHAND
Director
Development Fund
University of Montreal

HUGH A. BENHAM, LL.D.
Executive Director
The Winnipeg Foundation

J. LAURENCE BLACK
President
J.L. Black & Sons Ltd.

G.A. COSTANZO
Vice Chairman
First National City Bank

HON. LOUIS P. GÉLINAS
Consultant
Geoffrion, Robert & Gélinas Ltd.

JOHN T. JOHNSON, Q.C.
Partner
Borden & Elliot

HOWARD T. MITCHELL
President
Mitchell Press Limited

ALFRED T. SEEDHOUSE
Chairman
The Manufacturers Life
Insurance Company

RONALD D. SOUTHERN
President
Atco Industries Ltd.

H. ARNOLD STEINBERG
Executive Vice-President
Administration and Finance
Steinberg's Limited

H. HEWARD STIKEMAN, Q.C.
Senior Partner
Stikeman, Elliott, Tamaki,
Mercier & Robb

JOHN H. TAYLOR
Chairman
North American Life
Assurance Company

EDWARD D.H. WILKINSON, Q.C.
Partner
Russell & DuMoulin

WALTER B. WRISTON
Chairman
First National City Bank

G.A. COSTANZO
Chairman

PAUL H. AUSTIN
President

HON. LOUIS P. GÉLINAS
Vice-President

ALFRED T. SEEDHOUSE
Vice-President

DUNCAN CAMPBELL
Vice-President
Ontario Division

JOHN E. CLEGHORN
Vice-President
Western Division

WALTER A. PRISCO
Vice-President
Eastern Division

L. LINTON REID
Vice-President
Investment & Exchange

T. SEAN AHERN
General Manager and
Chief Accountant

E. EDWARD FULCHER
General Manager
Investment and Exchange

HAROLD F. HENRY
General Manager
Credit

G. STEVENS LYNCH
Secretary

JOHN E.G. MORRIS
Chief Inspector

WILLIAM T. LIVINGSTONE
Senior Supervisor
Personnel and Public
Relations

PRESIDENT'S ADDRESS



Paul H. Austin, President



Walter B. Wriston, Chairman

The Chairman has already mentioned that today's Annual General Meeting, being held away from the city of our Head Office, is a first for the Bank and perhaps for the industry. We intend to continue in this manner; it will be our goal in future years to hold these meetings in a number of cities across Canada. We want to give clients and shareholders the opportunity to meet and talk with our Directors and management. This approach follows the practice as far as our Board Meetings are concerned. These are held monthly in cities where Mercantile branches are located, reflecting our national character and representation across Canada. For instance, during the last year, five of eleven meetings were held outside of Montreal and again on these occasions our Directors were able to have contact with clients and community leaders.

The Bank experienced a good year in 1973 — a year when the economy was buoyant and favoured business expansion. Understandably, without our service oriented staff, whose performance has been excellent, and a growing clientèle, who have given one of the newer banks on the street a chance to prove its worth, the good progress recorded would not have been possible. I would like to take this opportunity to thank our officers and staff for the fine results, and on the other side of the equation, our clients, for the business they have directed to us.

Since the beginning of our share issue programme in March 1972, growth has been substantial. Growth, in many instances, can be disruptive and cause diverse organizational stresses: but, I am pleased to report to you that this has not been our experience. Our management team is a stable one; turnover in this group was only 10% last year. This stability has helped to afford excellent operating efficiency, as reflected in our year-end financial statement.

During 1973, the Bank's total assets increased by more than 50%, indicating a growth rate that was more than twice that of

the bank industry average of 24%. This increase in business reflected favourably on our income statement; total revenue increased by 68.5% due to an increase of interest sensitive assets, a higher average prime rate over 1972, improved exchange earnings, and a higher level of fees and commissions. On the expense side, non-interest expenses increased by only 15% during the year, as our continuing efforts to exercise tight cost controls were maintained. Interest costs rose by an exceptionally high 103% because of larger deposits to fund our assets, as well as higher deposit interest rates. In spite of these higher rates, Mercantile increased its balance of revenue — the banking industry's equivalent of earnings before income tax — by 39.1%. This compares to a 16.3% growth in balance of revenue recorded by the industry as a whole.

Notwithstanding this noteworthy earnings increase, two share issues during the year caused significant dilution of 64.5% in shareholders' equity. Nevertheless, our earnings per share declined only 11.3% from 95.2 cents a year ago to 84.4 cents in 1973. This is significant to shareholders, as it is tangible indication of the Board's and management's commitment to make certain that growth and profitability go hand in hand.

The stock issues I am referring to were the second and third in our programme of six that follows the accord with the Federal Government in 1971. We commenced these in early 1972, and are committed to finalize them by the end of 1980. At present, we are almost two-thirds of the way through. Each issue of one million shares legally raises the asset ceiling under which we operate by \$100 million. Investor reception at the time of each issue has been very encouraging. As I am sure you know, we are at present finalizing our fourth issue; in fact, a week tomorrow our new asset ceiling will be at the \$700 million level.

Although mentioned from time to time by the Bank's management, we find that one important aspect of our balance sheet structure is frequently overlooked by the investing public; namely, we are over-capitalized as compared to the industry average. The assets of our competitors tend to be around thirty times aggregate equity capital, while we are obliged by legislation to limit assets to a maximum of twenty times authorized capital. Without this restriction, and given our 1973 year-end total equity of \$34 million, and using the bank industry norm, we could grow to just over \$1 billion in assets, instead of being limited to our ceiling of \$600 million.

Once the final sixth issue is placed, our assets will be twenty times issued capital, which will work out to be about fifteen times total equity; thus, without further dilution, we shall be able to expand and double our footings, using, of course, the banking industry norm of thirty times. This means that earnings per share should show a very satisfactory growth



curve in the years following the last issue, to the benefit of our shareholders.

An indicator of the Bank's acceptance and success in the marketplace is the increase in our share of business loans — in September 1971 it was 1.65% of total outstanding bank business loans, 1.95% in September 1972 and 2.44% last September. Considering that our assets, at \$587 million, represented only 0.8% of total Canadian chartered bank assets at the end of October 1973, this growth is indeed encouraging. If we examine business loans according to size, we find that we now handle over 5.6% of these loans between \$1 million and \$5 million, and 3.8% of all business loans greater than \$1 million. Our loan portfolio is well diversified with most sectors of the economy represented.

As you know, our aim is to have a presence in the major commercial centres of Canada. In line with this goal, and in order to increase our participation in the Ontario market, we have recently opened a branch in Kitchener/Waterloo and will inaugurate another in Hamilton in April of this year. We have one other new branch in the final stages of completion, in Saint John, New Brunswick. As well, during 1973 our Winnipeg and Calgary offices were moved to more prestigious premises in locations better suited to our type of business. Additionally, I am pleased to report to you today that we have received approval from the California State banking authorities to open a representative office in the city of Los Angeles.

We are, of course, continually investigating new services that should be added to our product line. In early 1974 we will enter the residential mortgage market. Until now, we have concentrated on providing interim construction financing to developers of residential dwellings, with other lenders providing the longer term funds. After extensive study and preparation, we are now in a position to offer residential mortgages as a complement to our construction financing. We will continue

Mercantile's Board of Directors at one of the monthly meetings.

to assess new service opportunities and look for ways to create new sources of earnings for our Bank.

I would like to take a moment now to look at business prospects for the current year. As you know, the views of economists regarding 1974 have, in the recent past, been quite divergent. The common thread, however, is that the industrial world's strong economic performance in 1973 will not be matched in 1974. Closer to home, most economists and businessmen are now forecasting a slowdown in Canada's growth, and even if Canada's economy outperforms that of most other nations, as I believe it will, we cannot expect to avoid being affected by unfavourable world economic conditions. What is really at issue, is the magnitude of the forecast slowdown, and in this regard I tend to be optimistic. In 1974 we will continue to see prices rising too rapidly, unemployment too high, production levels again pushed to near capacity in most industries, and commodity shortages continuing. Despite these generally negative factors, it is my belief that the predictions of those who estimate that Canada's economy will experience real growth in the area of 5% in 1974 will be close to the final results. This expectation is based on a number of fairly well known factors: the Arab oil cutbacks will only decrease G.N.P. growth in the area of ½%; consumer and business capital spending will remain buoyant; exports will not drop as sharply as some expect due to Canada's relatively strong energy and raw material position; and unfilled orders, which are about \$7 billion in the manufacturing sector alone, add an underlying strength to the situation. In terms of loan demand in 1974, my views parallel those concerning economic growth; that is, there will be a slowdown in loan demand but that the magnitude of the slowdown will not be large.

Interwoven in all of this are market interest rate structures. In Canada, the prime lending rate in 1973 was artificially low for some time in relation to short term deposit rates, and our Bank experienced a profit squeeze in the latter part of our fiscal year and, I might add, into the first quarter of the current fiscal year. Interest rates should, however, gradually return to more normal relationships and to lower levels by mid 1974, with a corresponding improvement in our spreads during this period.

It would be appropriate at this point if I commented on our reliance on the money market for a large portion of our deposits. Mercantile Bank has, at present, nine branches, and while within the next few months we shall have expanded this to eleven, these branches are located in key commercial and financial areas and, as such, do not provide large savings balances. Without having this base of deposits generated at the branch level, we presently rely on the money market to fund some 60-75% of our assets. During the past years, and perhaps particularly in 1973, other banks and financial institutions have also been using the money market funding route to a greater extent, so that Mercantile's situation is by no means entirely unique.

In addition, significant changes have occurred in the marketplace in recent times, with a number of new corporate and financial firms relying on the money market as a source of funds. This, along with the increased requirements of traditional users, has significantly expanded the market, demonstrating that the volume of funds available has a direct relationship to the needs of the market, since appropriate rate differentials can attract funds from competing users. Really, it is simply a matter of rate — at the right price funds will be available to a creditworthy borrower. In addition, borrowers have access to the vast U.S. and European markets, and can thus draw on the savings of a much wider community than Canada. Traditionally, however, high market rates have been unsustainable, and when the rates turn down, as we expect they will, Mercantile, as I have said before, will be in a relatively good position to benefit from this decline.

In summary then, we are starting 1974 in a period of uncertainty; apart from the energy crisis and its effect on the economy, rate structures have not yet normalized. But in today's world, conditions change rapidly. With this in mind, and appreciative of Canada's potential in the industrial world, I am confident that, when 1974 is viewed in its entirety, Mercantile Bank will have maintained an acceptable growth in assets and earnings.

MINUTES OF THE TWENTIETH ANNUAL GENERAL MEETING

MINUTES of the Twentieth Annual General Meeting of the Shareholders of The Mercantile Bank of Canada held at the Royal York Hotel, Toronto, on Thursday, the 10th day of January, 1974, at 11:00 o'clock of the forenoon.

The Chairman of the Bank, Mr. Walter B. Wriston, presided and the Secretary, Mr. G.S. Lynch, acted as Secretary of the Meeting.

The notice of the Meeting having been sent to all Shareholders entitled to receive it and a quorum being reported present, the Chairman declared the Meeting to be duly convened and constituted.

With the consent of the Meeting, the Chairman appointed Mr. D. Charlebois and Mr. S.G. Hart to act as Scrutineers.

Upon motion of Mr. A. Bachand, seconded by Mr. H.T. Mitchell and carried, the Minutes of the last Annual Meeting held on January 11, 1973, were taken as read and confirmed.

The Chairman then asked the Secretary to read the Directors' Report to the Shareholders, omitting the Annual Statement and the Auditors' Report as these had already been sent to all Shareholders and copies were in the hands of those present.

Directors' Report

The Directors take pleasure in submitting to the Shareholders the Annual Statement of the Bank for the year ended October 31, 1973, together with the Auditors' Report.

During the year, two issues of the Bank's stock of 1,000,000 shares each were successfully marketed thereby raising to \$600,000,000 the limit imposed by the Bank Act on the size of the Bank's assets. The expansion in operations which was thus made possible is reflected in the Balance Sheet and the Statement of Revenue, Expenses and Undivided Profits. The sale of another issue of 1,000,000 shares, the fourth such issue, will be concluded in the next few days and this issue, like the previous ones, will enable the Bank to further increase its assets.

The number of branches has been increased to nine by the opening of one at Kitchener in late November. It is the intention to open two additional branches during the current year.

With much regret, the Directors report that Mr. S.C. Eyre, who has represented Citibank on the Board since 1969, will not stand for re-election this year. Mr. Eyre's devoted interest in the Bank's affairs and his wise counsel have been much appreciated; he will be greatly missed.

The loyal and efficient services of the staff are gratefully and sincerely acknowledged.

(Signed) Walter B. Wriston
Chairman

Montreal, January 10, 1974

The Chairman said that before moving the adoption of the Directors' Report he would ask the President to address the Meeting. (The President's Address is reproduced on pages three to five.)

It was moved by the Chairman and seconded by Mr. E.D.H. Wilkinson —

THAT the Directors' Report to the Shareholders, including the Annual Statement and the Auditors' Report thereon, in respect of the Bank's fiscal year ended October 31, 1973, be and the same is hereby approved and adopted.

The Chairman proposed that the ballot on this motion be taken later in the Meeting.

Amendment of Shareholders' By-Law I

In introducing this subject, the Chairman said —

"The next item of business concerns the date of the Annual Meeting. At present, our By-Laws provide that the Annual Meeting shall be held on the second Thursday of January in each year. It is felt that more flexibility in this matter would be desirable and your Directors recommended that the By-Law be amended to provide that the Annual Meeting be held on a date to be determined each year by the Directors but within the period specified by the Bank Act."

It was moved by Mr. J.T. Johnson and seconded by Mr. H.A. Benham that the following resolution be adopted —

THAT Shareholders' By-Law I be and is hereby repealed and replaced by the following —

The annual general meeting of the shareholders of the Bank for the election of directors and for the transaction of such other business as may properly be brought before the meeting shall be held on a day to be determined each year by the directors which shall be a day not more than fifteen months after the holding of the last annual general meeting. If the day so determined for the holding of any annual general meeting shall be declared a legal holiday, the meeting shall be held on the next following business day which is not a legal holiday.

The Chairman proposed that the ballot on this motion be taken later in the Meeting.

Auditors

It was moved by Mr. J.H. Taylor and seconded by Mr. J.L. Black —

THAT Mr. John S. Grant, C.A. and Mr. John F. Lewis, C.A. be appointed auditors of the Bank for the current year and that their remuneration in that capacity be not more than \$33,500.

Directors

In proposing that the election of Directors be proceeded with, the Chairman said —

"There has been no change in the composition of the Board since the last Annual Meeting but, as you learned from the Directors' Report, Mr. S.C. Eyre will not stand for re-election this year. Mr. G.A. Costanzo, Vice Chairman of Citibank, will be proposed for election as a Director to replace Mr. Eyre as one of Citibank's representatives on the Board."

At the Chairman's request, the Secretary then read the names of the persons proposed for election as Directors, namely: P.H. Austin, A. Bachand, H.A. Benham, J.L. Black, G.A. Costanzo, L.P. Gélinas, J.T. Johnson, H.T. Mitchell, A.T. Seedhouse, R.D. Southern, H.A. Steinberg, H.H. Stikeman, J.H. Taylor, E.D.H. Wilkinson, W.B. Wriston.

Mr. E.J. McConnell then nominated the persons whose names had been read by the Secretary for election as Directors of the Bank for the ensuing year.

The Chairman then directed that a ballot be taken on the motions to adopt the Directors' Report, to amend Shareholders' By-Law I, to appoint Auditors and for the election of Directors. Upon receiving the report of the Scrutineers, the Chairman declared that the resolutions adopting the Directors' Report, amending Shareholders' By-Law I and appointing Auditors had been duly passed and that the persons whose names had been read by the Secretary, and duly nominated, had been elected Directors.

The Meeting then terminated.

G.S. Lynch
Secretary

Walter B. Wriston
Chairman

At the subsequent meeting of the Board of Directors the following officers were elected:

Chairman, G. A. Costanzo; President, P. H. Austin; Vice-Presidents, L. P. Gélinas and A. T. Seedhouse.

STATEMENT OF ASSETS AND LIABILITIES

as at October 31, 1973
(with comparative figures for 1972)

Assets	1973	1972
Cash and due from banks	\$ 14,417,706	\$ 15,831,958
Cheques and other items in transit, net	9,573,476	186,278
Total cash resources	<u>23,991,182</u>	<u>16,018,236</u>
Securities issued or guaranteed by Canada, at amortized value	25,934,195	9,180,781
Securities issued or guaranteed by provinces, at amortized value	3,168,429	1,552,190
Other securities, not exceeding market value	53,469,253	14,201,078
Total securities	<u>82,571,877</u>	<u>24,934,049</u>
Day, call and short loans to investment dealers and brokers, secured	14,850,000	13,850,000
Other loans, including mortgages, less provision for losses	436,070,000	319,102,363
Total loans	<u>450,920,000</u>	<u>332,952,363</u>
Bank premises, at cost, less amounts written off	1,772,181	1,767,449
Customers' liability under acceptances, guarantees and letters of credit as per contra	25,515,104	13,254,107
Other assets	<u>2,473,760</u>	<u>1,077,874</u>
	<u>\$587,244,104</u>	<u>\$390,004,078</u>

See accompanying notes to financial statements.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the statement of assets and liabilities of The Mercantile Bank of Canada as at October 31, 1973 and the statements of revenue, expenses and undivided profits, accumulated appropriations for losses and rest account for the year ended on that date. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, the foregoing statements present fairly the financial position of the Bank as at October 31, 1973 and the revenue, expenses, changes in undivided profits, changes in accumulated appropriations for losses and transactions in the rest account of the Bank for the year ended on that date.

Montreal, Quebec
November 29, 1973

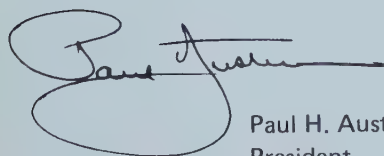
J.S. Grant, C.A.
of Peat, Marwick, Mitchell & Co.
J.E. Maheu, C.A.
of Maheu, Noël, Anderson, Valiquette et Associés

Liabilities	1973	1972
Deposits by Canada	\$ 4,114,700	\$ 1,214,538
Deposits by provinces	23,510,869	12,145,524
Deposits by banks	39,703,646	92,093,196
Personal savings deposits, payable after notice in Canada in Canadian currency	4,302,513	5,296,036
Other deposits	450,523,920	240,245,491
Total deposits	<u>522,155,648</u>	<u>350,994,785</u>
Acceptances, guarantees and letters of credit	25,515,104	13,254,107
Other liabilities	2,929,725	3,478,898
Total liabilities	<u>550,600,477</u>	<u>367,727,790</u>
Accumulated appropriations for losses	<u>2,637,779</u>	<u>2,280,354</u>


Shareholders' equity

Capital (Note 1):

Authorized—6,000,000 (1972—4,000,000) shares, par value \$5 each; issued and fully paid—5,000,000 (1972—3,000,000) shares	25,000,000	15,000,000
Rest account	8,498,300	4,674,000
Undivided profits	507,548	321,934
Shareholders' equity	<u>34,005,848</u>	<u>19,995,934</u>
	<u>\$587,244,104</u>	<u>\$390,004,078</u>



Paul H. Austin
President



T. Sean Ahern
for Chief General Manager

NOTES TO FINANCIAL STATEMENTS

October 31, 1973

- By Order in Council dated February 23, 1971, the Government of Canada approved a Special By-Law increasing the authorized capital of the Bank from \$10,000,000 to \$40,000,000 in stages of \$5,000,000 each. The first such increase became effective on the date of the Order in Council and each successive increase shall occur only after the additional shares created by the previous issue shall have been offered to and subscribed for by, or otherwise disposed of to, residents of Canada in compliance with the Bank Act. On each of March 30, 1972, December 14, 1972 and June 18, 1973, the Bank issued an additional 1,000,000 shares and consequently the authorized capital was increased to \$20,000,000, \$25,000,000 and \$30,000,000 respectively. At November 29, 1973, the Bank is in the process of making the fourth such issue of an additional 1,000,000 shares to residents of Canada which, when completed, will have the effect of increasing the authorized capital to \$35,000,000.

Notes continued on page 10

STATEMENT OF ACCUMULATED APPROPRIATIONS FOR LOSSES

For the Financial Year Ended October 31, 1973
(with comparative figures for 1972)

	1973	1972
Accumulated appropriations at beginning of year:		
Tax-paid—from amounts not subject to income tax	\$ 1,603	\$ 1,603
General	<u>2,278,751</u>	<u>1,706,437</u>
Total	2,280,354	1,708,040
Add (deduct):		
Appropriation from current year's operations, net of income taxes related thereto as set out below	200,000	150,000
Provision for losses on loans based on five-year average loss experience (included in other operating expenses) less the loss experience on loans for the year	(19,323)	271,353
Profits and losses on securities, including provisions to reduce securities other than those of Canada and its provinces to values not exceeding market	(28,252)	961
Income tax credit related to appropriation from current year's operations (Note 2)	<u>205,000</u>	<u>150,000</u>
Accumulated appropriations at end of year	<u>\$2,637,779</u>	<u>\$2,280,354</u>
Tax-paid (amounts not subject to income tax)	\$ 1,603	\$ 1,603
General	<u>2,636,176</u>	<u>2,278,751</u>
	<u>\$2,637,779</u>	<u>\$2,280,354</u>

See accompanying notes to financial statements.

STATEMENT OF REST ACCOUNT

For the Financial Year Ended October 31, 1973
(with comparative figures for 1972)

Balance at beginning of year	
Premium on issuance of capital stock	
Expenses of issue, net of income taxes relating thereto (Note 2)	
Balance at end of year	

See accompanying notes to financial statements.

- By an Order in Council of the Government of Canada dated October 30, 1973, the presentation of appropriations for losses and income taxes in the Statement of Revenue, Expenses and Undivided Profits and in the Statement of Accumulated Appropriations for Losses by chartered banks has been changed. The effect has been to develop the balance of revenue after provision for income taxes and then separately deduct from that figure, on an after-tax basis, the appropriation for losses to arrive at the balance of profits for the year. The income tax reduction related to the tax deductible amount of appropriation for losses has been segregated in the Statement of Accumulated Appropriations for Losses. The figures for 1972 have been reclassified to conform with the method of presentation used in 1973. The aggregate provision for income taxes is made up as follows:

In respect of Balance of Revenue	
In respect of current appropriations for losses (credit)	
In respect of expenses of capital stock issues (Rest Account)	

STATEMENT OF REVENUE, EXPENSES AND UNDIVIDED PROFITS

For the Financial Year Ended October 31, 1973
(with comparative figures for 1972)

	1973	1972		1973	1972
..	<u>\$4,674,000</u>	<u>\$3,000,000</u>	Revenue:		
..	<u>4,000,000</u>	<u>1,750,000</u>	Income from loans	<u>\$36,138,972</u>	<u>\$21,654,146</u>
..	<u>175,700</u>	<u>76,000</u>	Income from securities	<u>2,620,348</u>	<u>1,157,102</u>
	<u>3,824,300</u>	<u>1,674,000</u>	Other operating revenue	<u>3,099,738</u>	<u>2,029,571</u>
..	<u>\$8,498,300</u>	<u>\$4,674,000</u>	Total revenue	<u>41,859,058</u>	<u>24,840,819</u>
			Expenses:		
			Interest on deposits	<u>28,033,069</u>	<u>13,802,058</u>
			Salaries, pension contributions and other benefits	<u>3,432,453</u>	<u>3,024,282</u>
			Property expenses including depreciation	<u>1,256,339</u>	<u>1,193,799</u>
			Other operating expenses, including provision for losses on loans based on five-year average loss experience	<u>2,596,714</u>	<u>2,117,287</u>
			Total expenses	<u>35,318,575</u>	<u>20,137,426</u>
			Balance of revenue	<u>6,540,483</u>	<u>4,703,393</u>
			Provision for income taxes relating thereto (Note 2)	<u>2,756,000</u>	<u>2,095,000</u>
			Balance of revenue after provision for income taxes	<u>3,784,483</u>	<u>2,608,393</u>
			Appropriation for losses, net of income taxes related thereto (Note 2)	<u>200,000</u>	<u>150,000</u>
			Balance of profits for the year	<u>3,584,483</u>	<u>2,458,393</u>
			Dividends	<u>3,398,869</u>	<u>2,275,000</u>
			Amount carried forward	<u>185,614</u>	<u>183,393</u>
			Undivided profits at beginning of year	<u>321,934</u>	<u>138,541</u>
			Undivided profits at end of year	<u>\$ 507,548</u>	<u>\$ 321,934</u>
			Balance of profits per share based on average shares outstanding	<u>84.4¢</u>	<u>95.2¢</u>

See accompanying notes to financial statements.

	1973	1972
....	<u>\$2,756,000</u>	<u>\$2,095,000</u>
....	<u>(205,000)</u>	<u>(150,000)</u>
....	<u>(179,605)</u>	<u>(71,363)</u>
	<u>\$2,371,395</u>	<u>\$1,873,637</u>

AN ANALYSIS OF THE BANK'S OPERATIONS

The following analysis is presented in order to help the shareholder appraise the performance of Mercantile Bank.

Assets and Liabilities

Total Assets of \$587,244,104 at the end of October, 1973 were up 50.6% from a year ago while loans rose by 35.4% to \$450,920,000 in the same twelve month period. This compares with a total bank industry growth in assets and loans of 23.7% and 23.0% respectively. Mercantile's loans grew at a rate less than that of assets due to a large rise in holdings of securities which rose by 231.2% from \$24,934,049 at the end of 1972 to \$82,571,877 at the end of the latest fiscal year. While government securities rose \$18,369,653 (171.2%) reflecting an increase in liquidity, "Other Securities" increased by 276.5% (\$39,268,175) to \$53,469,253 resulting, in part, from the Bank's increase in holdings of corporate securities, the income from which is tax free. These securities take the form of income debentures and have a favourable effect on the Bank's after tax yield. Total Loans accounted for 76.8% of the Bank's assets compared with the banking industry's figure of 57.7% for fiscal 1973 thus demonstrating the importance of the generally higher yielding loans in Mercantile's profit mix.

Total Deposits to fund the Bank's assets, at \$522,155,648, were up 48.8% from a year earlier, a lower rate of growth than for Total Assets due primarily to two rights issues, which increased the Bank's equity in fiscal 1973 by \$14 million to \$34,005,848. Acceptances, Guarantees and Letters of Credit almost doubled from \$13,254,107 at the end of 1972 to \$25,515,104 on October 31, 1973.

Profit and Loss

Total Revenue for the year at \$41,859,058 grew by \$17,018,239 or 68.5% from 1972, reflecting both increases in interest sensitive assets and an increased prime rate as well as improved exchange earnings and higher fees and commissions over 1972.

Taking each item of revenue separately, Income from Loans rose by 66.9% to \$36,138,972, an increase of \$14,484,826 for the year as a result of both higher volume and an increase of 102 basis points in Mercantile's average prime rate. Income from Securities at \$2,620,348 was up \$1,463,246 or 126.5% over 1972. This high growth was largely due to an increase in holdings of "Other Securities". The actual yield on Total Securities was virtually unchanged between 1972 and 1973 owing to the increased proportion of lower yielding instruments in the securities portfolio in 1973 as discussed under Assets and Liabilities above. The rise in Other Operating Revenue of 52.7% reflects an increase in fees and commissions as well as in foreign exchange income.

Total interest income (Total Revenue less Other Operating

Revenue) grew by 69.9% over 1972 to \$38,759,320. However, interest paid on deposits rose by 103.1% to \$28,033,069 causing Mercantile's net interest earnings to increase by only 19.1% to \$10,726,251 from \$9,009,190 in 1972. There were basically two factors contributing toward this relatively low growth rate. Firstly the structure of interest rates during the year was unfavourable in that money market rates increased greater than the prime during the year. Secondly there was a large component of low yielding tax free interest earnings from income debentures in Income from Securities. If the revenue from the latter were grossed up to a pre-tax equivalent net interest earnings would have shown significantly higher growth. Because of the environment of rising deposit rates the Bank's yield-cost spread¹ narrowed significantly during the year.

Non-interest expenses — all expenses other than interest on deposits — increased by 15.0% to \$7,285,506 in 1973. The items included in this category are those concerning salaries and staff benefits, property, and other operating expenses. Salaries and related benefits increased by \$408,171 or 13.5% to \$3,432,453 reflecting an increase in staff (necessary for the Bank's expanded operations) from 328 to 367 at the comparative fiscal year ends. Property Expenses at \$1,256,339 were up only 5.2% over the 1972 level. This increase reflects the costs of the Montreal branch and Head Office new premises which were occupied for only part of the year in 1972 and new locations for Mercantile's Calgary and Winnipeg branches. The new branch in Kitchener had very little effect in 1973 in that the branch opened late in the fiscal year.

Other Operating Expenses at \$2,596,714 rose by \$479,427 or 22.6% over the 1972 level. A number of items were responsible for the advance. The provision for loan losses based on five-year average loan loss experience which is charged against the Other Operating Expense account increased significantly due entirely to the increase in loan volume. The five-year average loan loss as a percent of loans was approximately one tenth of 1%, a ratio below that of 1972. Travel expenses rose but not only as a result of increased customer related travel but also as a result of staff relocation and the training programme which involves bringing officers from all over the country to Head Office. Owing to the rise in the number of shares outstanding (two stock issues were made in fiscal 1973) common stock registration fees rose. As well, an in-house computer was installed at the end of the 1972 fiscal year causing increases in automation expenses during 1973. Finally, as a result of taxation changes, including the introduction of a capital tax in British Columbia and a change in the basis of calculation in Ontario, there was a rise in the amount of business and provincial taxes paid during the year.

Mercantile's Balance of Revenue, which is the bank industry's earnings before income tax, rose by 39.1% in 1973 to \$6,540,483 from \$4,703,393 at the end of 1972. Were the tax free revenue mentioned earlier grossed up to reflect its tax free nature the Balance of Revenue growth would be a little more in line with the 50% growth of year-end assets demonstrating that Mercantile's productivity overcame its lower spread on earning assets. Even without this, Mercantile's 39% growth in profits exceeded the total banking industry's figure of 16.3%.

As explained in Note 2 of the financial statements, as of this year all chartered banks are required to state their balance of revenues taxed at the effective rate of the institutions; where there are tax free appropriations for loss the actual taxes paid are reduced accordingly. Provision for Income Taxes increased by \$661,000 or 31.6% over the restated 1972 provision making the effective 1973 tax rate 42.1% compared with 44.5% in 1972. Tax free revenue from income debentures was the primary reason for the effective tax rates being lower than the statutory rates.

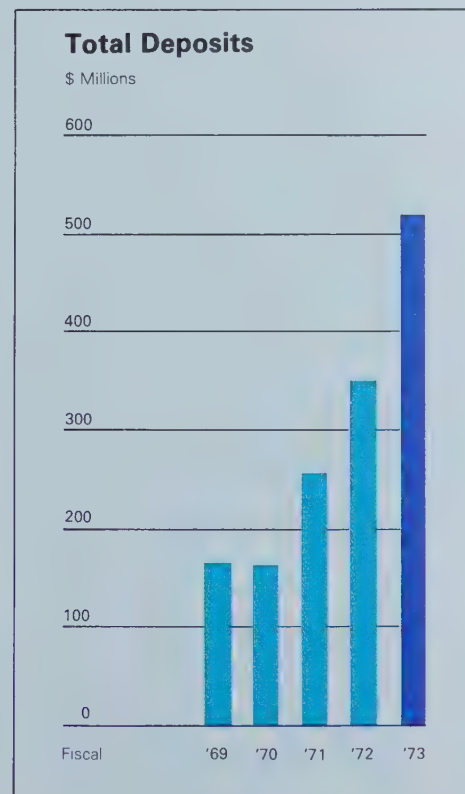
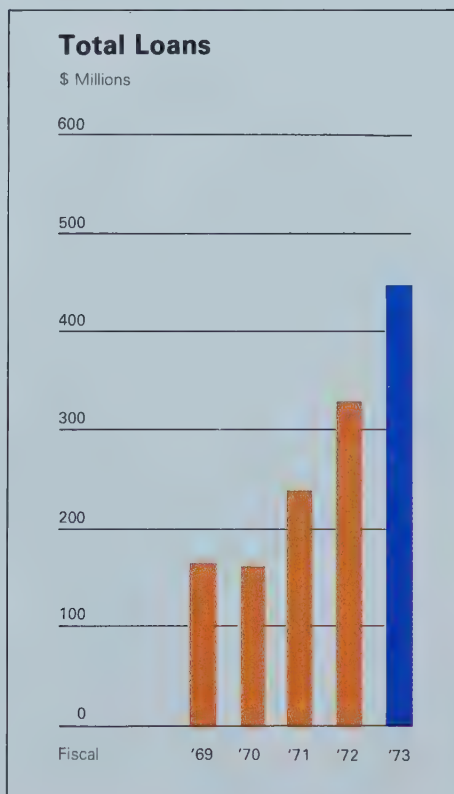
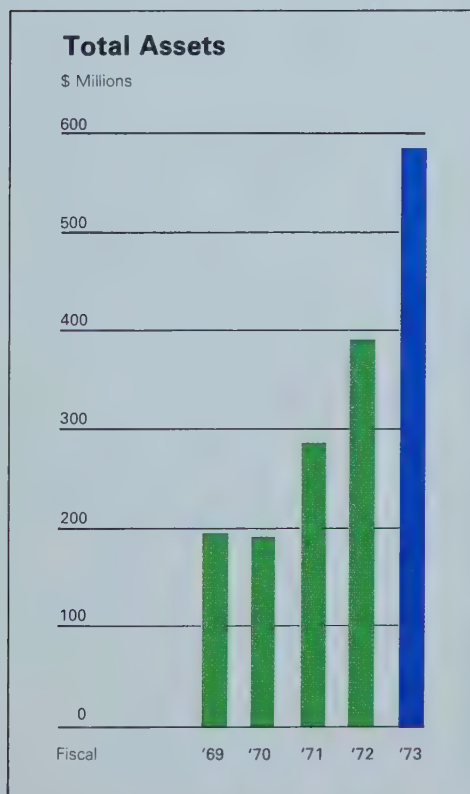
Appropriations for Losses, a provision made for possible loan

loss, now shown on an "after-tax" basis in accordance with the new reporting format, rose by 33.3% to \$200,000 over the restated \$150,000 of 1972. This reflects the Bank's increased loan volume in 1973. On a pre-tax basis the amounts were \$405,000 in 1973 and \$300,000 in 1972.

After deducting taxes and appropriations for losses the Balance of Profits for the year amounted to \$3,584,483 compared with \$2,458,393 at the end of 1972. The increase of 45.8% was higher than the increase for the Balance of Revenue because of the lower effective tax rate in 1973. As well, the growth in Balance of Profits of 45.8% was higher than that of average interest sensitive assets growth (42.9%) again demonstrating Mercantile's productivity which offset the reduced spreads of 1973.

Total dividends paid in 1973 amounted to \$3,398,869 compared with \$2,275,000 in 1972. Dividends in 1972 were paid on 2,000,000 shares for the first quarter and on 3,000,000 shares for the remaining three quarters, while in 1973 they were paid on 4,000,000 shares in the first half of the year and on 5,000,000 in the remainder. The regular dividend rate for 1973 was 50 cents per share with a special

FIVE YEAR LOOK AT BALANCE SHEET HIGHLIGHTS



dividend of 23 cents declared at year-end. The total amount paid out in 1973 amounted to 94.8% of the total Balance of Profits for the year compared with a rate of 92.5% in 1972. This is in accordance with the Bank's present policy to distribute some 90% of its profits to shareholders.

The Balance of Profits per average share outstanding was 84.4 cents on 4,249,315 average shares in 1973 versus 95.2 cents on 2,583,333 average shares in 1972. This dilution of 64.5% caused by the issue of new shares was a main contributor to the drop in earnings per share in 1973 from 1972.

Productivity

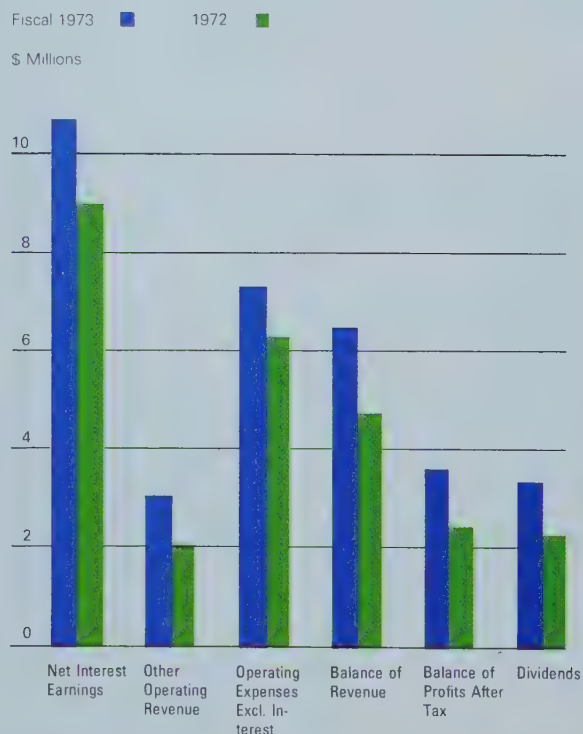
A factor that helped Mercantile perform well, in spite of high money costs and narrowing spreads is the Bank's productivity. Loans per employee amounted to \$1,229,000 and \$1,003,000 at the end of 1973 and 1972 respectively. The comparative all bank figures were approximately \$387,000 and \$348,000.

Another important measure is that of non-interest operating expenses as a percentage of net interest earnings. Mercantile's ratios in the last two years of 67.9% in 1973 and 70.3% in 1972 compare very favourably with the banking industry figures of 82.6% and 81.7%. Again if the tax free income were grossed up for the tax effect this figure would be even more favourable.

In terms of return on assets (Balance of Revenue as a percentage of total average assets on a monthly basis), this ratio was 1.33% and 1.38% in 1973 and 1972 respectively for Mercantile compared with 1.16% and 1.18% for the total banking industry.

¹ The yield-cost spread is the difference between the yield on interest sensitive assets and the interest cost of total deposits plus debentures.

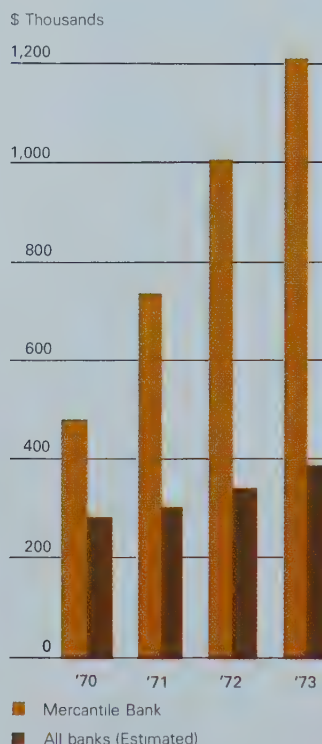
PROFIT AND LOSS HIGHLIGHTS



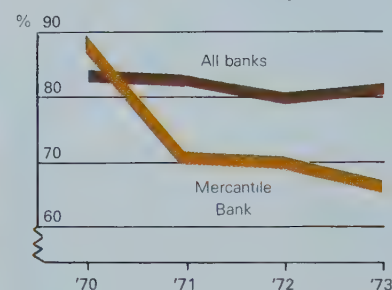
PRODUCTIVITY

Fiscal year-end

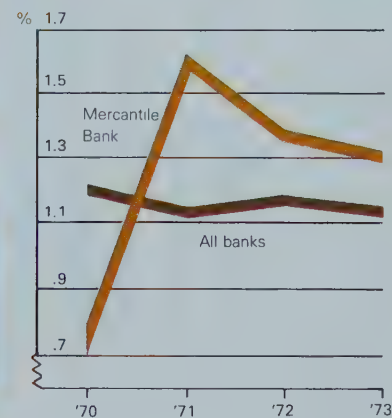
Loans per Employee



Operating Expenses / Net Interest Earnings



Return on Assets



FOCUS ON MERCANTILE BANK

Figures by themselves do not indicate the type of enterprise an institution is. Mercantile is a Canadian chartered bank offering all the conventional banking services. However, we are continuing our policy of concentrating on commercial business; both Directors and management alike are aware of our responsibilities to the marketplace and will continue to enlarge services where appropriate. Our branches are spread across Canada from coast to coast where we offer a variety of services to our customers and speedily implement them with our short and direct lines of communication between the field and our regional offices.

The chart on this page illustrates Mercantile's wide representation in all facets of Canada's commercial activities. Be it natural resources, industry, construction or other fields, Mercantile Bank is able to give corporations advice and assistance not only on the domestic scene but also internationally, through our affiliation with First National City Bank.

A BREAKDOWN OF OUR 1973 LOAN PORTFOLIO

MANUFACTURING

TRANSPORTATION

FOOD, BEVERAGES AND TOBACCO

MORTGAGES AND PERSONAL LOANS

CONTRACTORS

NATURAL RESOURCES

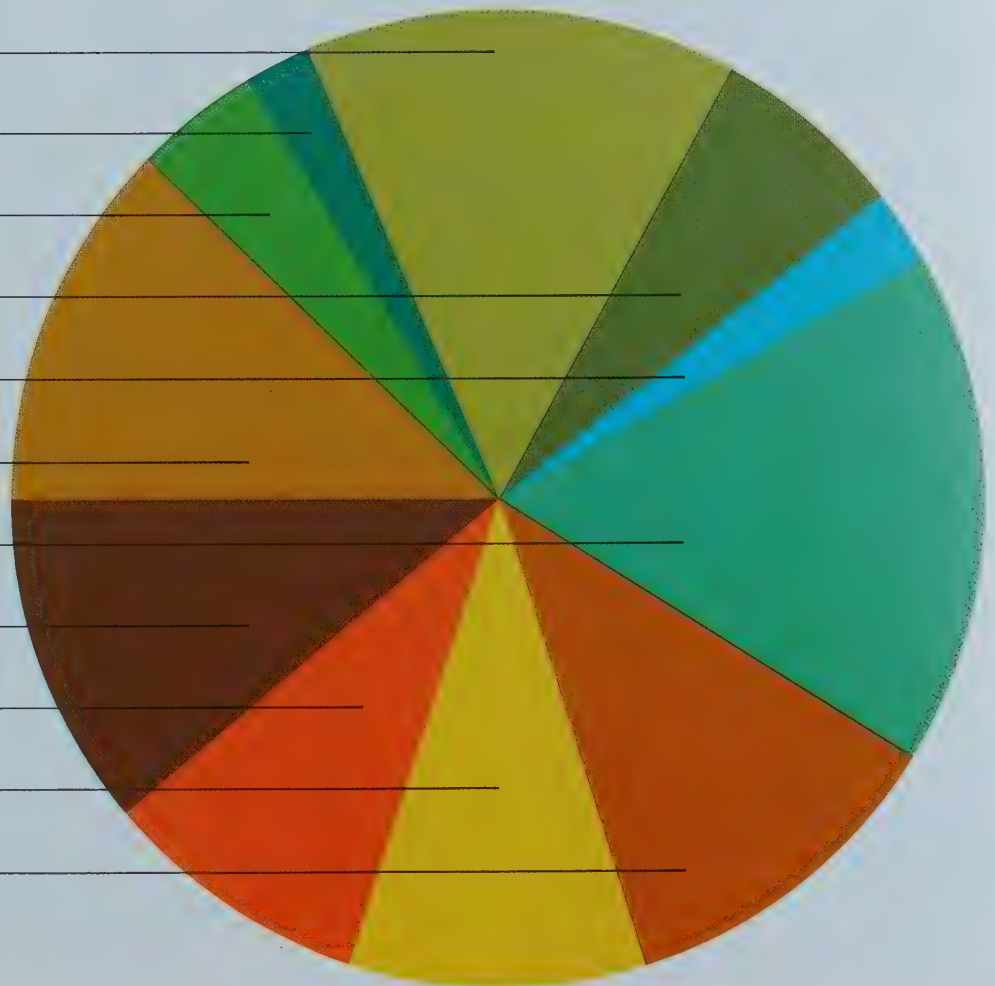
REAL ESTATE, INTERIM CONSTRUCTION FINANCING
AND RELATED INDUSTRIES

GOVERNMENT AND PUBLIC SERVICES,
AGRICULTURE AND OTHERS

MERCHANDISING

PUBLIC UTILITIES

FINANCIAL INSTITUTIONS



We strive to keep in close contact with our clients to assure them the best possible service and at the same time to develop new relationships. Apart from our main services, we also offer those in specialized fields. These include our Computer Assisted Financial Analysis, or CAFA; with the input of company data we are able to produce a variety of types of financial analyses and projections for the client. This not only assists us in evaluating our customers' financial requirements but also can be used by the firms themselves as a tool in forward planning. Through our affiliation with Citibank, we can help companies find new connections, be it for import or export purposes or for the search of an acquisition or merger, in over ninety countries and in even more locations with the assistance of correspondent banks.

At present Mercantile Bank has nine branches situated in key commercial centres across Canada — stretching from Halifax to Vancouver. With such representation we feel we are able to service all areas of the Canadian economy.

Natural resources are perhaps Canada's greatest asset giving the country the ability not only to benefit from their extraction and sale, but also from the creation of secondary industry around them and the resultant possibility of exporting these products. The natural resource sector is significant to the Bank which is involved in financing mining, petroleum, forestry, agriculture and their ancillary products.

As an example, our Vancouver branch is active in assisting a sector of the forest products industry by supplying working capital for inventory and term loans for construction of new mills. In addition, this also involves equipment financing for the barges and tugs used, and export financing of the finished lumber to overseas and eastern United States markets.

In the pulp industry, our Eastern Division played an important role in revitalizing a depressed area in Quebec. Until almost two years ago a pulp mill had been the main source of employment in Temiscaming. Then it was closed. However, just a few months ago, the mill was re-opened by another company, in co-operation with the Quebec Government, the Federal Government, the people of Temiscaming, the mill's old and new employees, and Mercantile Bank.

The Prairie economy is in the midst of a major boom. Our Winnipeg branch is active in assisting agriculture. At a time when the availability of agricultural equipment was far less than the demand, Mercantile Bank was playing a major role in assisting implement manufacturers in restructuring their financial requirements in order to meet the sales potential of their farm machinery.

Good lines of transportation are vital to a country as large and disparate as Canada. Whether road, rail, air or water, Mercantile is playing its part in this area of Canada's development. On both the east and west coasts we are servicing clients with tug boat fleets. Vessel construction and term financing was recently provided by our Halifax office for one of the largest ocean going tugs on the Canadian east coast. Furthermore,

Mercantile has been active in financing the development of natural resource industries:



Finished lumber is loaded in Vancouver for overseas destinations.



The Tembec paper mill in Temiscaming, Quebec.



Two Co-operative Implements' combines in full swing on the Prairies.



The retail market is also served by Mercantile — here customers carry out their business in Quebec City.



Mercantile's services to the shipping industry are exemplified by its financing of this large east coast tug.



In the North:
financing construction of the new Explorer Hotel, Yellowknife, N.W.T.



Providing term loan financing for new drilling rigs.



Mercantile assists a growing yogurt producer.



Kraus Carpets is one of the largest manufacturers of carpets in Canada and a customer of our Kitchener/Waterloo branch.



Corporate managers discuss new plant expansion in the Canadian distilling industry.



The Bank is involved in financing portable housing, here seen on the assembly line.



Finance of research and development is vital. Mercantile is assisting Gen Tec Inc. in experiments concerning lasers.

despite the fact that there is no water nearby, the manufacture of tugs and barges is being carried out in Edmonton. Our officers there were involved in financing a steel fabrication plant that manufactured this type of transportation equipment. After construction these units are cut into sections and shipped north where they are re-welded and put to use on the Mackenzie River.

Although still in its infancy, the development of Canada's northern areas is becoming increasingly significant to the country's economy. Mercantile is assisting Keen Industries Ltd.'s exciting growth in its various activities in the North, including heavy construction, truck, barge and air transportation, and drilling and related oil field services.

As the North opens up, indeed even at its initial stages of development, accommodation is a basic requirement. Our Edmonton branch is providing financing for the new Explorer Hotel in Yellowknife scheduled to open in May 1974.

Mercantile Bank has entered into partnership with federal and provincial government agencies to provide financial assistance to fast-growing medium-size companies. Typical of this situation is Delisle Yogourt Ltd. The yogourt and related canned pudding business has been in a stage of rapid development for the past few years. Mercantile has supported Delisle's exceptional expansion and growth programme. Much of their success revolves around the introduction of their Swiss style, fruit flavoured yogourt, and the abilities of Mercantile Bank to develop and co-ordinate the financing needed to stimulate the company's growth.

Sometimes financing that involves large denominations is arranged by means of a number of institutions joining together. Recently a joint venture financing of a new office building in Edmonton was arranged between Mercantile and the Alberta Treasury Branches.

Our Bank's versatility in financing is noteworthy in construction and real estate financing. While also providing operating credit facilities to corporations in this business, we have found that our services in the field of real estate project financing has been of particular assistance in the areas of term and

construction lending. We are involved in many sectors of the industry, ranging from the provision of interim financing for a major downtown convention centre to assistance in the financing of the construction of bridges. A major residential project at present concerning our Halifax office is that of Cowie Hill Village. On a fifty-five acre site overlooking the city, this development consists of 439 condominium town-houses, high- and low-rise apartments and a community centre. The project is primarily being funded under Central Mortgage and Housing Corporation's innovative housing and assisted home ownership programmes with additional financing being provided by conventional lenders.

A rapidly growing area of the construction industry is that of portable housing. The world's largest manufacturer of industrial portable accommodation is Atco Industries, a public company, based in Calgary. We provide primarily term financing to Atco whose products are sold worldwide.

Secondary and manufacturing industry is an important sector of the Canadian economy. Mercantile Bank is also playing its part in this area. Lord & Cie, structural steel contractors and manufacturers of roof deck siding and cellular decking under the trademark of Lordeck, is one of Canada's largest manufacturers in this innovative field. The Bank has assisted the company by providing for its daily operative requirements and for the direct financing of its capital expenditure programmes.

The textile industry is labour intensive and as such an important source of employment, especially in the province of Quebec. Mercantile is active in a number of ways in this industry including the ecological aspect. Liberty Wool Stock Company Ltd. is one of Canada's leading wholesalers of textile waste products while a division, Liberty Spinning Mills, produces yarn. These complementary activities function primarily around the recycling of textile waste products, being unused waste portions of fabric generated by garment manufacturers, old discarded clothing and substandard synthetic fibres from textile fibre producers. The Bank is assisting Liberty in its growth and expansion programmes and has also serviced the customer's import and export requirements through our worldwide facilities.

As well as being active in the primary stages of the textile industry, we are also involved in the manufacture of finished textile goods. Our youngest branch, in Kitchener/Waterloo, has arranged a financial package of current and term loan financing for Kraus Carpets. These funds were used to purchase equipment to develop the company's extruding operation, employed to process the polypropylene-based raw material into a textured yarn.

A major manufacturing and servicing industry that is in the growth stage is that concerning computers. Computrex Centres Ltd., based in Calgary, sells, services and leases computer peripheral equipment and is a Canadian leader in several areas of the computer graphics business. Mercantile provides Computrex with financing of the company's lease sales as well as equipment financing.

Research is an essential prerequisite of industry. In the highly specialized electrical and electronic manufacturing industry we are financing Gen Tec Inc. in their experiments on industrial uses for the gas laser.

Mercantile Bank is pleased with its long association with the internationally renowned distiller, Bacardi, having been involved with the company's Canadian operations located near Toronto since its inception. Mercantile financed part of the original plant and equipment and now we are financing related new operations.

Fishing is another important sector of Canada's food industry. Our activity in this field on both the east and west coasts emphasizes our representation right across Canada. Mercantile's working capital financing for fish inventory and generated sales is provided to the Pacific salmon industry in Vancouver. And, in the Maritimes, our credits finance the groundfish and shellfish industry. Term financing assistance is also extended for vessels, plant and equipment required by one of the largest fish and lobster processing plants in the Atlantic provinces. While most of the lobsters are sold for the table, many are processed into a wide range of canned and frozen products for the retail and restaurant trades.

As an economy develops, the significance of the service industries increases. One such service with which we are associated is advertising. We provide assistance to Claude Neon, specialists in outdoor advertising and sign manufacturing. Recently Claude Neon announced details of a five year project aimed at upgrading outdoor advertising in order to improve the appearance of Canadian cities and towns.

These are a few examples of the types of commerce we service. As Mercantile Bank expands we look forward to doing more for Canadian business and the part we can play in Canada's growth.

Financing fishing East and West:



Lobsters processed in the Maritimes.



Salmon caught in the Pacific.



Claude Neon are pioneering a project in Canada to give a facelift to outdoor advertising.

HEAD OFFICE AND BRANCHES

HEAD OFFICE

625 Dorchester Boulevard West
Montreal, Quebec H3B 1R3

BRANCHES

Eastern Division

Montreal:
625 Dorchester Blvd. West

John E. Pierce,
Manager

Quebec City:
580 Grande Allée East

Gilles Seguin,
Manager

Halifax:
1 Sackville Place

James S. Parsons,
Manager

Ontario Division

Toronto:
120 Adelaide Street West

Geoffrey D. Farrar,
Manager

Kitchener:
22 Frederick Street

James A. W. Van Slyck,
Manager

Western Division

Vancouver:
1177 West Hastings Street

Brian McL. Romer,
Manager

Calgary:
441, 5th Avenue, S.W.

Peter Hewlett,
Manager

Edmonton:
10030 Jasper Avenue

John R. Groves,
Manager

Winnipeg:
305 Broadway Avenue

Maurice M. Christens,
Manager



Mercantile Bank of Canada

Affiliated with First National City Bank
